

1
2
3
4
5
6
7
8 IN THE UNITED STATES DISTRICT COURT
9 FOR THE NORTHERN DISTRICT OF CALIFORNIA
10

11 IN RE: No C-02-1550 VRW
12 PACIFIC GAS and ELECTRIC CO, (Bankruptcy Case No 01-30923 DM)
13 Appellant, Cross-
14 Appellee, Debtor and Chapter 11 Case
Debtor in Possession
15 Federal ID No 94-0742640 ORDER
16

17 PG&E appeals from a March 18, 2002, order of the
18 bankruptcy court, entitled "Order and Judgment Disapproving
19 Disclosure Statement; Rule 54(b) Certification" (bankruptcy order),
20 which embodies a ruling issued on February 7, 2002, entitled
21 "Memorandum Decision Regarding Preemption and Sovereign Immunity"
22 (bankruptcy decision). Doc #1. On June 24, 2002, the court denied
23 a motion to dismiss PG&E's appeal filed by The People of the State
24 of California, the California Public Utilities Commission (CPUC)
25 and the City and County of San Francisco (collectively, objectors).
26 Doc #68. The court determined that the bankruptcy court's FRCP
27 54(b) certification was proper and, consequently, that appellate
28

1 jurisdiction exists as of right, pursuant to 28 USC § 158(a)(1).
2 In the alternative, the court granted PG&E's "protective" motion
3 for leave to file an interlocutory appeal, pursuant to section
4 158(a)(3), determining that in the event the bankruptcy court's
5 FRCP 54(b) certification was not proper, the court would still
6 exercise its discretion to hear this appeal.

7 This appeal poses a discrete question of statutory
8 interpretation of tremendous importance to one of the largest
9 bankruptcies in United States history.

10
11 I

12 This matter, like many others currently in federal court
13 and in this district, including an action filed by PG&E against the
14 CPUC, is tied to California's attempt to restructure its regulatory
15 scheme for the generation and sale of electricity. In PG&E v
16 Lynch, 01-3023-VRW, 2002 US Dist LEXIS 13895 (July 25, 2002), the
17 undersigned discussed at length California's statutory scheme
18 implementing this restructuring, the energy crisis beginning in the
19 summer of 2000 and the resulting effects on PG&E. The court will
20 not repeat this discussion here, although it provides the backdrop
21 for PG&E's bankruptcy and the instant appeal.

22 On April 6, 2001, claiming that the combination of the
23 energy crisis and the retail rate freeze enacted as part of
24 California's restructuring scheme had ruined its credit rating and
25 led to "billions of dollars in defaulted debt and unpaid bills,"
26 PG&E Br (Doc #14) at 5, PG&E filed a voluntary petition under
27 chapter 11 of title 11 of the United States Code (bankruptcy code)
28 in the United States Bankruptcy Court for the Northern District of

1 California. On December 19, 2001, PG&E and its parent company
2 filed their first amended plan (December plan) of reorganization
3 and their first amended disclosure statement. See ER at 153, 207.

4 Central to the December plan is the disaggregation of
5 PG&E, which involves the creation of three new limited liability
6 companies and the separation of PG&E's operations into four lines
7 of business, reflecting PG&E's historical functions: retail gas
8 and electric distribution; electric transmission; interstate gas
9 transmission and electric generation. As a result of the
10 reorganization contemplated by the plan, four companies, all
11 subsidiaries of PG&E's parent company, would emerge from
12 bankruptcy: ETrans, containing PG&E's electric transmission
13 assets; GTrans, PG&E's gas transmission assets; Electric Generation
14 (Gen), PG&E's generation assets; and the Reorganized PG&E, which
15 would continue in the retail sale and distribution of electricity
16 and gas. According to PG&E, the entities involved in electric
17 transmission, interstate gas transmission and electric generation
18 will no longer be subject to the regulatory jurisdiction of the
19 CPUC after reorganization, but will be under the exclusive
20 ratemaking jurisdiction of the Federal Energy Regulatory
21 Jurisdiction (FERC). The Reorganized PG&E would remain under the
22 CPUC's regulatory jurisdiction, subject, however, to the limits
23 imposed upon that jurisdiction by federal law. See PG&E v Lynch,
24 01-3023-VRW, 2002 US Dist LEXIS 13895.

25 Absent preemption, state law poses a formidable obstacle
26 to the execution of several of the central transactions required to
27 carry out the plan. For example, a critical feature of the plan is
28 the transfer of PG&E's retained generation to the new limited

1 liability company, Gen. According to the CPUC, however, such a
2 transfer of generation assets would be illegal under California
3 Public Utilities Code § 377, enacted in January 2001, which
4 prohibits an owner of electric generation facilities from disposing
5 of any such facilities until January 1, 2006. The CPUC also
6 contends that several of the critical transactions proposed in the
7 plan require state regulatory review and approval under state
8 health, safety, welfare and environmental statutes, including the
9 California Environmental Quality Act (CEQA). Under California
10 Public Utilities Code § 851, for example, PG&E would ordinarily be
11 required to obtain state approval to sell, lease or spin off its
12 utility facilities. According to the CPUC, an application for such
13 approval requires an environmental review under CEQA.

14 As noted in this court's June 24 order, the CPUC objected
15 to PG&E's disclosure statement in the proceedings below. The CPUC
16 asserted that the proposed reorganization (1) impermissibly sought
17 to preempt state and federal law not subject to preemption and (2)
18 sought declaratory and injunctive relief against California in
19 violation of principles of sovereign immunity. In response to the
20 former objection (the latter is not at issue in this appeal), PG&E
21 asserted that all state--and most if not all other non-bankruptcy--
22 laws are expressly preempted by § 1123(a)(5) of the bankruptcy code
23 insofar as they purport to prohibit, veto or nullify transactions
24 necessary to implement the restructuring proposed in the plan.
25 Pursuant to § 1123(a)(5), PG&E asserted that a confirmation order
26 approving its plan and authorizing the transactions contemplated by
27 the plan would:

28 //

preempt "otherwise applicable nonbankruptcy law" in the following areas: (1) any approval or authorization of the CPUC or compliance with the California Public Utilities Code or CPUC rules, regulations or decisions otherwise required to transfer public utility property (including authorizations to construct facilities), issue securities and implement the Plan; and (2) the exercise of discretion by any other state or local agency or subdivision to deny the transfer or assignment of any of the Debtor's property, including existing permits or licenses, or the issuance of identical permits and licenses on the same terms and conditions as the Debtor's existing permits and licenses where both the Reorganized Debtor and one or more of ETrans, GTrans and Gen requires such permit or license for their post Effective Date operations.

First Am Disc Statement (ER 346).

Notably, PG&E contends that the preemption authorized by § 1123(a) occurs "at the time the Plan is implemented." Id. In other words, PG&E does not contend that its reorganization plan has the effect of preempting application of nonbankruptcy law that would apply to the reorganized PG&E and the new entities after reorganization. Rather, PG&E explicitly concedes that the four companies emerging from bankruptcy will be subject to all applicable state and federal law on a going-forward basis. Moreover, PG&E states that it intends to follow "the established procedures for the transfer of most permits and licenses," as many of these procedures are "ministerial or governed by objective criteria that make it unlikely that the agency or subdivision could act or fail to act in a way that would interfere with consummation of the Plan." Id. PG&E seeks to be free only from nonbankruptcy requirements that threaten the reorganization provided for in the plan. To be sure, PG&E's concern that, absent some form of preemption, state actors such as the CPUC could exercise a veto over PG&E's proposed reorganization is not without basis.

1 Throughout its brief filed in this matter, the CPUC makes clear its
2 displeasure not just with PG&E's attempt to evade state regulatory
3 processes, but with the goal PG&E is pursuing and, in particular,
4 the transfer of regulatory control from the state to FERC over
5 several of PG&E's lines of business. According to the CPUC this is
6 not a desirable outcome, as "federal regulation is not an adequate
7 substitute for state regulation on many practical levels." CPUC Br
8 (Doc #78) at 13.

9 On February 7, 2002, the bankruptcy court issued its
10 memorandum decision regarding preemption and sovereign immunity,
11 rejecting PG&E's "across-the-board, take-no-prisoners" claim that §
12 1123(a)(5) allows it to "disaggregate with unfettered preemption of
13 any contrary nonbankruptcy law." Bankr Dec (ER 863) at 46, 40. In
14 a lengthy decision, the bankruptcy court rejected

15 the notion that Congress, without a hint in the
16 legislative history in a section of the Bankruptcy Code
17 entitled "Contents of Plan," and using words calling for
18 "adequate means for the Plan's implementation," intended
19 to permit a debtor's plan--confirmed by a bankruptcy
20 judge (not by legislative act, as in most preemption
21 situations)--to obliterate a whole area of jurisdiction
22 and authority traditionally left to state law.

23 Id at 22-23.

24 Although rejecting PG&E's claim that nonbankruptcy laws
25 otherwise applicable to the restructuring transactions proposed in
26 the plan were expressly preempted by the bankruptcy code, the
27 bankruptcy court did not, however, finally determine that state
28 laws operating as impediments to PG&E's proposed reorganization
could not be preempted under principles of implied preemption.
Indeed, the bankruptcy court expressed its "belie[f] that the Plan
could be confirmed if Proponents are able to establish with

1 particularity the requisite elements of implied preemption;" and
2 noted that "[i]f the Disclosure Statement is amended consistent
3 with this Memorandum Decision, the court will approve it and let
4 the Proponents test preemption at confirmation." Id at 3. The
5 bankruptcy court directed PG&E to identify, as part of its attempt
6 to show implied preemption, the laws it wished to preempt and "to
7 state in summary fashion" why the laws should be preempted. Id at
8 40.

9 Recognizing the centrality of the issue it decided, the
10 bankruptcy court certified its decision for immediate appeal,
11 pursuant to FRCP 54(b), made applicable to bankruptcy proceedings
12 by Fed R Bankr P 7054(a) and Fed R Bankr P 9014:

13 This is a Chapter 11 case of enormous significance to
14 thousands of creditors owed billions of dollars. It is
15 clearly one of the largest bankruptcies in United States
16 history, and definitely the largest involving a public
17 utility. An attempt by a utility to free itself from
18 state regulation to the extent contemplated by the Plan
19 is virtually without precedent. Further, PG&E expects to
pay creditors in full with interest, but already this
case is nearly a year old and further delay should be
avoided. Creditors have a real economic interest in a
speedy resolution of this case. If a court on appeal
believes that express preemption is available here, the
rule of law should be settled forthwith.

20 Bankr Order (ER 924) at 5-6.

21 As noted, this court determined that certification was
22 proper. The bankruptcy court's judgment is, therefore, properly
23 before the court, pursuant to 28 USC § 158(a)(1). This appeal
24 poses essentially a single question of statutory interpretation.
25 The bankruptcy court's interpretation of the bankruptcy code is
26 reviewed de novo. See, e g, Tighe v Celebrity Home Entm't, Inc.,
27 210 F3d 995, 997 (9th Cir 2000).
28

II

A

In relevant part, § 1123(a) provides:

(a) Notwithstanding any otherwise applicable nonbankruptcy law, a plan shall--

* * *

(5) provide adequate means for the plan's implementation, such as--

* * *

(B) transfer of all or any part of the property of the estate to one or more entities, whether organized before or after the confirmation of such plan;

The court first notes that, although it may sometimes seem so from the parties' briefs and the oral arguments at the hearing on this appeal, this is not a matter of deciding whether § 1123(a) expressly preempts some nonbankruptcy law or impliedly preempts some bankruptcy law. There is, in fact, no question that § 1123 expressly preempts some nonbankruptcy law--both parties agree that the "notwithstanding" phrase has some express preemptive meaning--the dispute is over which laws are preempted and in what context. With respect to this dispute, the parties' interpretation of the statutory section differ widely.

The CPUC contends, and the bankruptcy court essentially agreed, that § 1123 is merely a "directive" statute, specifying in subsection (a) thereof what must be put in a reorganization plan and in subsection (b) what may be put in a reorganization plan. The purpose of the section is to require "that adequate information be provided that would enable a hypothetical investor typical of holders or claims or interests of a relevant class to make an

1 informed judgment about the plan." Bankr Dec at 22. Under this
2 interpretation, the central phrase in dispute, "[n]otwithstanding
3 any otherwise applicable nonbankruptcy law," merely clarifies that
4 "the debtor's obligation to set forth adequate means for the plan's
5 implementation in the proposed plan may not be altered or varied by
6 any nonbankruptcy law." CPUC Br (Doc #78) at 20. This phrase then
7 is rather innocuous, adding little to the provisions of the
8 section. Indeed, notwithstanding its apparent application to all
9 paragraphs in subsection (a), the CPUC is not completely convinced
10 that "[t]he 'notwithstanding' phrase * * * applies to section
11 1123(a)(5) at all." Id.

12 PG&E contends, by contrast, that § 1123 does not merely
13 clarify what must and may go into a plan, but substantively
14 empowers debtors to engage in certain actions unfettered by
15 otherwise applicable nonbankruptcy laws, including all the means by
16 which the plan may be implemented specified in § 1123(a)(5). In
17 short, § 1123(a)(5) preempts all nonbankruptcy laws "that are
18 obstacles to the transactions and steps necessary to effect a
19 reorganization plan." PG&E Br (Doc #14) at 3. Under this
20 interpretation, state laws and regulators may not stand as an
21 impediment to the restructuring provisions of a chapter 11 plan of
22 reorganization, although these laws will again apply to the
23 reorganized debtor and any new entities created pursuant to the
24 plan.

25 The California Hydropower Reform Coalition (CHRC) and the
26 United States Environmental Protection Agency (EPA) have both
27 weighed in on the subject. See Docs ##70 and 74. The CHRC
28 essentially mimics the CPUC's position. The EPA, although noting

1 that PG&E has "stated that [it] intend[s] to comply with all
2 federal regulatory laws and obtain all federal approvals necessary
3 to implement its proposed plan," asserts that, in its view, PG&E's
4 interpretation of the preemptive effect of § 1123(a) is too broad.

5 PG&E is, however, indeed correct that its interpretation
6 of § 1123(a) is consistent with that of every court to address the
7 issue, except, of course, the bankruptcy court below. After
8 careful consideration, the court is convinced that the bankruptcy
9 court's determination that § 1123(a) merely directs the debtor to
10 place certain items in its reorganization plan is erroneous.
11 Rather, a review of the text and legislative history of this
12 section demonstrates that Congress intended expressly to preempt
13 nonbankruptcy laws that would otherwise apply to bar, among other
14 things, transactions necessary to implement the reorganization
15 plan.

16
17 B

18 The CPUC contends that, in interpreting § 1123(a), the
19 court should apply the so-called "presumption against preemption"
20 and that this presumption operates in favor of the CPUC's proposed
21 interpretation. In support of this argument, the CPUC centrally
22 relies on Medtronic, Inc v Lohr, 518 US 470 (1996), in which the
23 Supreme Court discussed the proper approach to "interpreting a
24 statutory provision that expressly pre-empts state law." Id at
25 484. The Court noted that interpretation of express preemption
26 language "does not occur in a contextual vacuum," but is rather
27 informed by "two presumptions about the nature of pre-emption." Id
28 at 485.

First, because the States are independent sovereigns in our federal system, we have long presumed that Congress does not cavalierly pre-empt state-law causes of action. In all pre-emption cases, and particularly in those in which Congress has "legislated * * * in a field which the States have traditionally occupied," Rice v Santa Fe Elevator Corp, 331 US 218, 230 (1947), we "start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." Ibid; [further citations omitted].

* * *

Second, our analysis of the scope of the statute's pre-emption is guided by our oft-repeated comment, initially made in Retail Clerks v Schermerhorn, 375 US 96, 103 (1963), that "the purpose of Congress is the ultimate touch-stone" in every pre-emption case.

Id at 485-486.

The two presumptions about the nature of preemption identified by the Court in Medtronic are often collapsed into one "presumption against preemption," which essentially stands for the proposition that state police powers are generally presumed not to be superseded absent indication that such preemption was the "clear and manifest purpose of Congress." See, e g, Hillsborough County v Automated Medical Laboratories, Inc, 471 US 707, 715 (1985).

The application of this presumption against preemption was recently discussed by the Supreme Court in New York v FERC, 122 S Ct 1012, 1023 (2002):

Pre-emption of state law by federal law can raise two quite different legal questions. The Court has most often stated a "presumption against pre-emption" when a controversy concerned not the scope of the Federal Government's authority to displace state action, but rather whether a given state authority conflicts with, and thus has been displaced by, the existence of Federal Government authority. See, e g, Hillsborough County v Automated Medical Laboratories, Inc, 471 US 707, 715 (1985)(citing cases); see also Medtronic, Inc v Lohr, 518 US 470, 485 (1996); Cipollone v Liggett Group, Inc, 505 US 504, 518 (1992). In such a situation, the Court "starts with the assumption that the historic police

1 powers of the States were not to be superseded * * *
 2 unless that was the clear and manifest purpose of
 3 Congress.'" Hillsborough County, 471 US at 715 (quoting
 4 Jones v Rath Packing Co, 430 US 519, 525 (1977)).
 These are not such cases, however, because the question
 presented does not concern the validity of a conflicting
 state law or regulation.

5 Id at 1023.

6 As noted by the Court in New York v FERC, the presumption
 7 against preemption is commonly applied in order to determine
 8 whether particular state laws are either expressly preempted by a
 9 federal statute or impliedly preempted by federal regulation in a
 10 given field. The question of the validity of a particular state
 11 law in light of express or implied preemption by Congress, however,
 12 is not the question posed by the instant appeal. Rather to resolve
 13 this appeal the court must choose between two radically different
 14 arguments about what sort of laws Congress meant expressly to
 15 preempt. This determination cannot be made based on a presumption,
 16 but must be made in terms of ordinary principles of statutory
 17 construction. Once this choice is made, and the "purpose of
 18 Congress," Medtronic, 518 US at 486, is clarified, then the
 19 presumption against preemption may become relevant--although this
 20 is somewhat doubtful given the seemingly broad reach of the
 21 "notwithstanding" phrase--in order to determine whether a
 22 particular state law is preempted. But to apply the presumption
 23 against preemption to determine Congress' intent would be to place
 24 the cart before the horse.

25 Rather than beginning with a presumption, therefore, as
 26 an initial matter at least, the court must look to the plain
 27 language of the statute. See, e g, Exxon Corp v Hunt, 475 US 355
 28 (1986).

C

As noted, every court except the bankruptcy court below to have considered § 1123(a)(5) has concluded that this section contains an express preemption of nonbankruptcy laws that would otherwise apply to the restructuring transactions provided for in a reorganization plan. The case law on this subject is, however, rather limited. By far, the court to have considered this matter in the most depth is the United States Bankruptcy Court for the District of New Hampshire in Public Service Company of New Hampshire v New Hampshire (In re Public Serv Co), 108 BR 854 (D NH 1989). After conducting a quite helpful and thorough analysis of the (again rather limited) legislative history of § 1123(a), the New Hampshire bankruptcy court concluded that the meaning of § 1123(a)(5) is clear:

With regard to the present statutory provision before the court, i e § 1123(a)(5) providing that "notwithstanding any otherwise applicable nonbankruptcy law" a plan of reorganization "shall" contain adequate provisions for the plan's implementation, in terms of the necessary restructuring of the debtor and its assets and liabilities common to all plans of reorganization in complex cases, the statute would seem to be plain on its face to indicate an express preemptive intent as to such restructuring provisions of a chapter 11 plan of reorganization.

Id at 882.

Indeed, to the New Hampshire bankruptcy court, the conclusion "seems obvious" that § 1123(a)(5):

on its face contemplates that restructuring transactions necessary to a plan of reorganization may be provided notwithstanding nonbankruptcy law, and that upon confirmation of the plan pursuant to § 1129(a) of the Bankruptcy Code the confirmed plan--and the reorganized debtor created thereby--will be governed by those provisions.

Id.

Besides its thorough consideration of the precise question posed in the instant appeal, In re Public Serv Co is particularly interesting because it is quite factually similar to the situation here. That case too involved an electric utility debtor in reorganization, seeking to create new limited liability companies, some of which would no longer be under state regulatory control after reorganization, but would be under the jurisdiction of FERC. Similarly, the state commission in that case argued that its approval of the restructuring transactions was required by state law and the utility resisted submitting to this approval.

The New Hampshire bankruptcy court noted that its interpretation of the preemptive force of § 1123(a)(5) was also reached by the Fourth Circuit in Universal Cooperatives, Inc v FCX, Inc, 853 F2d 1149 (4th Cir 1988). In FCX, appellee Universal challenged an order of the bankruptcy court, affirmed by the district court on appeal, which, pursuant to § 1123(a)(5)(D), authorized FCX to release collateral securing its indebtedness to Universal in satisfaction of Universal's claim, in a manner that violated Universal's bylaws. Section 1123(a)(5)(D) provides that, "(a) notwithstanding any otherwise applicable nonbankruptcy law, a plan shall-- * * * (5) provide adequate means for the plan's implementation, such as-- * * * (D) sale of all or any part of the property of the estate either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate." Universal, to which FCX was in debt, had previously issued to FCX "patronage certificates" which were redeemable by Universal at the discretion of Universal's board of directors. FCX desired to

1 offset Universal's claim by the release of the patronage
2 certificates and contended that § 1123(a)(5)(D) preempted any
3 restrictions in Universal's bylaws applying to such a release. The
4 Fourth Circuit reasoned:

5 Because "Congress may * * * abrogate state law
6 entitlements in bankruptcy pursuant to its Bankruptcy
7 Clause Power, US Const, art I, § 8, cl 4," In re Farmers
8 Markets, 792 F2d 1400, 1403 (9th Cir 1986), we must ask
9 further whether there exists any conflicting bankruptcy
10 law which overrides the discretionary power over the
11 redemption of the patronage certificates vested in
12 Universal's board by state law and its by-laws. FCX here
13 contends that § 1123(a)(5)(D) preempts the restrictive
14 provisions of Universal's by-laws and allows it to
15 release the patronage certificates in satisfaction of
16 Universal's claim.

17 * * *

18 In 1984, the opening clause of § 1123(a) was amended to
19 read: "Notwithstanding any otherwise applicable
20 nonbankruptcy law, a plan shall * * *." By its plain
21 language then, § 1123(a)(5)(D) overrides nonbankruptcy
22 law restrictions on the distribution of collateral to
23 satisfy a claim secured by the same. Accordingly, §
24 1123(a)(5)(D) supersedes the discretionary power over
25 surrender of the patronage certificates bestowed on
26 Universal's board by its by-laws.

27 Id at 1154.

28 In the Ninth Circuit, too, the only case to address the
issue reached a similar conclusion of the preemptive effect of §
1123(a)(5). In In re Entz-White Lumber & Supply, Inc, 850 F2d 1338
(9th Cir 1988), the Ninth Circuit considered § 1123(a)(5)(G), which
as an example of "adequate means for the plans implementation,"
specifies the "curing or waiving of any default." Great Western
Bank & Trust (Great Western), an Arizona banking corporation,
objected to confirmation of a reorganization plan that provided for
the cure of debtor's default on a loan by Great Western by the
payment of the full principal balance owed as well as interest

1 accrued, at a rate of 1.5%. Great Western asserted that pursuant
2 to the terms of the loan agreement it was entitled to interest at
3 the rate of 18% per annum in the event of default. Debtor (Entz-
4 White) argued that its payment of the debt and interest under the
5 plan amounted to a "cure" of the default and that, pursuant to §
6 1123(a)(5)(G), this cure "nullified any consequences of the
7 default, including a post-maturity higher interest rate." Id at
8 1340.

9 The bankruptcy court, the district court and the Ninth
10 Circuit all ruled in favor of the debtor, accepting this argument.
11 The Ninth Circuit held:

12 [B]y curing the default, Entz-White is entitled to avoid
13 all consequences of the default--including higher post-
14 default rates. * * * It is clear that the power to cure
15 under the Bankruptcy Code authorizes a plan to nullify
16 all consequences of default, including avoidance of
17 default penalties such as higher interest.

18 Id at 1342.

19 As it is binding precedent, Entz-White would seem to be
20 the beginning and the end of the matter. The court of appeals
21 begins its opinion by stating that debtor's argument was made under
22 § 1123(a)(5)(G). Noting that this argument indeed "seems to
23 conform to the broad language of section 1123," the court of
24 appeals discusses § 1124(2), which determines whether a party is
25 impaired by a chapter 11 reorganization plan. Because of this
26 discussion, the CPUC contends that PG&E's reliance upon Entz-White
27 is "way off the mark." But the CPUC's attempt to distinguish the
28 case in this manner is "off the mark." The court of appeals
considered § 1124(2) at length, but only in response to Great
Western's argument that Congress intended in the bankruptcy code

1 "to allow debtors to cure only those defaults the consequences of
2 which are solely acceleration of the remaining payments due."
3 Entz-White, 850 F2d at 1340. The Ninth Circuit rejected this
4 argument by analyzing § 1124(2). More importantly, the Ninth
5 Circuit was not swayed from its belief that Entz-White's argument
6 that a cure provided for in the reorganization plan nullified any
7 consequences of default "conform[ed] to the language of section
8 1123." *Id.* Indeed, in this light, the most plausible explanation
9 for the Ninth Circuit's lack of an extended discussion of the
10 preemptive effect of § 1123 is that it--as did the New Hampshire
11 bankruptcy court and the Fourth Circuit--viewed the preemptive
12 effect of this section as evident and not requiring prolonged
13 discussion.

14 The court is aware of at least one other court holding
15 explicitly that it is "clear" that § 1123(a) affirmatively empowers
16 actions otherwise barred by nonbankruptcy law. See In re
17 Buttonwood Partners, Ltd, 111 BR 57, 59-60 (noting that "§ 1123
18 clearly contemplates that a plan may impair a class of claims
19 'notwithstanding any other applicable nonbankruptcy law;' an event
20 occurring here."). See also In re Public Serv Co, 108 BR at 89 n25
21 (listing other cases addressing § 1123(a)(5)).

22 In contrast, the court is not aware of a single case,
23 other than the decision challenged herein, holding that § 1123(a)
24 is merely a "directive" statute, preempting only nonbankruptcy laws
25 that might direct what should go in a reorganization plan. The
26 CPUC urges the court to follow the decision of the Ninth Circuit in
27 Baker & Drake v Public Serv Comm'n (In re Baker & Drake), 35 F3d
28 1348 (9th Cir 1994), and, indeed, this is the case given the most

1 attention by the bankruptcy court in the challenged order. Yet
2 Baker v Drake is simply not on point.

3 Baker & Drake (Baker), a taxicab operator employing
4 approximately 200 drivers, filed for chapter 11 bankruptcy. As
5 part of its reorganization plan, Baker proposed converting its
6 employee-drivers into independent contractors, who would lease the
7 cabs from Baker. As noted by the Ninth Circuit, "[t]his
8 arrangement would shift the ultimate control over taxi services
9 from Baker to the drivers themselves. Apart from the effect it had
10 on Baker's tort liability and insurance premiums, Baker stood to
11 save a good deal of money because it would no longer be liable for
12 payroll taxes." Id at 1350.

13 The problem, however, was that Nevada law prohibited
14 certified "common motor carriers," such as Baker, from leasing a
15 taxicab to another person and required "every driver of a taxicab
16 [to] be either the holder of a certificate or the employee of a
17 holder of a certificate.'" Id, quoting Nev Admin Code (NAC) §
18 706.371. Notwithstanding this prohibition, the bankruptcy court
19 "not only approved the proposed reorganization plan, but also
20 enjoined the Nevada Public Service Commission (PSC) from enforcing
21 NAC 706.371 against Baker," based on its determination that
22 Nevada's regulation of the taxi business conflicted with the
23 Bankruptcy Act's goal of fostering reorganizations. Id. Upon
24 appeal, the district court overturned this decision, holding that
25 the bankruptcy code did not preempt NAC 706.731 and vacated the
26 bankruptcy court's injunction.

27 The Ninth Circuit, in turn, quite sensibly affirmed this
28 decision, rejecting Baker's claim that "the Bankruptcy Act

1 impliedly preempts Nevada's regulation of taxi services," id at
2 1353 (emphasis added), because, among other things, NAC 706.371 is
3 "not just an economic regulation, but one reasonably intended to
4 secure the public convenience and safety" and, "[m]ore
5 importantly," because NAC 706.371 "does not directly conflict with
6 the purposes of the Bankruptcy Act in any way which could be
7 generalized beyond the facts of the present case." Id at 1354-55.

8 Baker & Drake is not an express preemption case. Baker
9 did not argue that NAC 706.371 was expressly preempted by §
10 1123(a)(5), or any other statutory provision, nor would it have
11 made sense to do so. Baker was seeking to preempt ongoing state
12 law, applying not to the transactions necessary for reorganization,
13 but to business activities engaged in by the reorganized debtor
14 after the reorganization. Accordingly, Baker & Drake is simply not
15 relevant to the instant appeal.

16 But the bankruptcy court's heavy reliance upon Baker &
17 Drake, see Bankr Dec at 12-17, does suggest why that court may have
18 been led astray. The bankruptcy court's decision seems to have
19 been guided by two primary concerns: the scarcity of legislative
20 history on the relevant statutory provisions and the concern that
21 construing § 1123(a)(5) to grant the right "to disaggregate with
22 unfettered preemption of any contrary nonbankruptcy law," id at 40,
23 would lead to "absurd results." Id at 19. The court will discuss
24 the legislative history of § 1123 below. But it is the bankruptcy
25 court's list of the supposedly absurd results of PG&E's urged
26 interpretation, which PG&E refers to as the bankruptcy court's
27 "parade of horrors," that demonstrate how the bankruptcy court
28 was misled. For each of these absurdities contemplates ongoing

1 illegality, such as that at issue in Baker & Drake, and not conduct
2 or action that is contemplated by PG&E in its restructuring plan.
3 The bankruptcy court was concerned, for example, that under PG&E's
4 interpretation a reorganization plan could approve the sale of
5 alcohol to minors, the dumping of toxic waste or the formation of a
6 monopoly. See Bankr Dec at 19. But such actions involve
7 contemplated ongoing illegality. In contrast, PG&E seeks the
8 suspension of nonbankruptcy law applying only to transactions
9 necessary for reorganization and does not contend that the
10 reorganized companies would be exempt from any laws on a going
11 forward basis by virtue of reorganization. The graphic but
12 undifferentiated nature of the illegalities that the CPUC contends,
13 and the bankruptcy court accepted, would follow from holding that §
14 1123(a) preempts nonbankruptcy obstacles to PG&E's reorganization
15 highlights the tenuousness of CPUC's position on this appeal.

16 The argument that absurd and/or undesirable consequences
17 flow from a particular statutory construction is of little direct
18 relevance to statutory construction. See, e g, New York State
19 Conference of Blue Cross & Blue Shield Plans v Travelers Ins Co,
20 514 US 645, 655 (1995)(in considering preemption claims, courts
21 "begin as * * * in any exercise of statutory construction with the
22 text of the provision in question, and move on, as need be, to the
23 structure and purpose of the Act in which it occurs."). Nor must
24 the court consider absurd consequences of a statutory construction,
25 potentially embraced by the literal language of an act, when the
26 matters at issue do "not test the margins of the Act" but "fall
27 within the heartland * * *." National Cable & Telecomms Ass'n Inc
28 v Gulf Power Co, 534 US 327, 122 S Ct 782, 790 (2002). Putting the

1 direct relevance of the "parade of horrors" to the court's task
2 of statutory interpretation aside, however, the court is
3 unconvinced that PG&E's interpretation of § 1123(a)(5) leads to
4 absurd or undesirable results.

5 As noted, the preemption of laws otherwise applicable to
6 restructuring transactions would not authorize ongoing illegality
7 by the reorganized debtor and any new entities created through
8 reorganization. Accordingly, in the unlikely event that a debtor
9 in bankruptcy would propose such things as the sale of alcohol to
10 minors or discharge of toxic wastes into waterways, this conduct
11 would be reachable by the same state and federal laws designed to
12 prohibit such conduct.

13 Moreover, the bankruptcy code contains several provisions
14 making it highly unlikely that reorganization plans contemplating
15 ongoing illegality would be seriously considered by the bankruptcy
16 court, much less confirmed in a plan of reorganization. Section
17 1123(a)(5) itself requires that reorganization plans contain
18 "adequate" means of implementation. Section 1129(a)(3) permits
19 confirmation of a reorganization plan by the bankruptcy judge only
20 if, among other things, it is proposed in "good faith," §
21 1129(a)(3), and "is not likely to be followed by the liquidation, or
22 the need for further financial reorganization, of the debtor or any
23 successor to the plan." § 1129(a)(11). The good faith test of §
24 1129(a)(3) has been interpreted to mean that "the plan was proposed
25 with 'honesty and good intentions' and with 'a basis for expecting
26 that a reorganization can be effected.'" Koelbl v. Glessing (In re
27 Koelbl), 751 F2d 137, 139 (2d Cir 1984), quoting Manati Sugar Co. v
28 Mock, 75 F2d 284, 285 (2d Cir 1935). See also Connell v Coastal

1 Cable TV, Inc, 709 F2d 762, 765 (1st Cir 1983)(to satisfy good
2 faith requirement, reorganization plan "must bear some relation to
3 the statutory objective of resuscitating a financially troubled
4 corporation."). The Ninth Circuit has interpreted § 1129(a)(11) to
5 "prevent confirmation of visionary schemes which promise creditors
6 and equity security holders more under a proposed plan than the
7 debtor can possibly attain after confirmation." Pizza of Hawaii,
8 Inc v Shakey's Inc (In re Pizza of Hawaii), 761 F2d 1374, 1382 (9th
9 Cir 1985), quoting 5 Collier on Bankruptcy, 15th ed, ¶ 1129.02 at
10 1129-34 (1984). A plan contemplating ongoing illegality, of
11 course, is quite likely to promise more than it can attain. These
12 provisions, among others, therefore, provide ample grounds for the
13 exercise of the bankruptcy court's discretion to refuse to confirm
14 plans contemplating ongoing illegality.

15 The CPUC also asserts that PG&E's interpretation of §
16 1123(a)(5) could, irrespective of illegality after reorganization,
17 shield debtors from laws designed to prohibit undesirable conduct
18 otherwise applying to the restructuring transactions themselves.
19 The CPUC argues, for example, that the preemption of laws otherwise
20 applicable to transactions necessary to carry out a reorganization
21 plan could permit anticompetitive mergers through reorganization,
22 which would otherwise violate § 7 of the Clayton Act, 15 USC § 18,
23 or analogous state laws, but which would not necessarily result in
24 the formation of a monopoly, prohibited by § 2 of the Sherman Act,
25 15 USC § 2. The CPUC and the EPA further argue that PG&E's proposed
26 statutory construction would permit debtors to evade such things as
27 certain laws requiring environmental review by regulators.

28 The requirements of § 1129(a)(3), of course, would apply

1 here as well, prohibiting confirmation of reorganization plans not
2 proposed in good faith. More importantly, however, the court
3 thinks that the CPUC's worst-case scenarios are rather more
4 equivocal than characterized by the CPUC. Consider, for example, a
5 corporate debtor that could reorganize in order to satisfy
6 creditors and emerge solvent by, among other things, merging with
7 another corporation. If such a merger would result in a monopoly
8 then a reorganization plan proposing it would be unlikely to be
9 confirmed. It is by no means clear, however, that a merger that
10 would perhaps have some anticompetitive impact reachable by § 7 of
11 the Clayton Act or some analogous state law, but which would not
12 result in a monopoly--and which would, moreover, rescue a debtor
13 from bankruptcy--would be undesirable.

14 Nor is the court convinced that the temporary suspension
15 of environmental review requirements that would otherwise apply to
16 (often somewhat fictional) restructuring transactions is
17 undesirable. In the instant case, for example, a CEQA review,
18 according to the CPUC, is triggered by transactions incidental to
19 PG&E's disaggregation. Permitting such review would permit state
20 regulators to exercise a veto over the restructuring of a utility
21 in bankruptcy, which could potentially impose a dramatic limitation
22 on PG&E's ability to reorganize despite the fact that no change
23 whatever were made to any PG&E operation. It is difficult for the
24 court to discern the countervailing consideration mandating the
25 ability of state regulators to exercise such power, when PG&E
26 itself has, presumably, already gone through CEQA review and the
27 four entities emerging from bankruptcy will be required to comply
28 with all applicable state and federal laws on an ongoing basis.

- 1
- 2
- 3
- 4
- 5
- 6
- 7
- 8
- 9
- 10
- 11
- 12
- 13
- 14
- 15
- 16
- 17
- 18
- 19
- 20
- 21
- 22
- 23
- 24
- 25
- 26
- 27
- 28

9

10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

1 propose a plan contrary to any law," concluded the bankruptcy
2 court, "Congress would not have treated the amendment as merely
3 'stylistic.'" Id at 25.

4 The language cited by the bankruptcy court accompanied
5 the first bill proposing the addition of the "notwithstanding"
6 phrase. This bill and a subsequent bill, also including the
7 proposed addition, failed. "The bill that finally became law arose
8 from a Senate bill that referred to this change as a 'technical
9 stylistic change []." S Rep No 65, 98th Cong, 1st Sess 84 (1983).
10 There are no committee reports with regard to the 1984 amendments,
11 but the change to § 1123(a)(5) was included verbatim from the prior
12 bills under a subtitle captioned "Miscellaneous Amendments." The
13 1984 Amendments came out of a conference committee with no report
14 other than the agreed-upon bill itself. On the floor the changes
15 including the change to § 1123(a)(5) were referred to as the
16 "technical amendments" subtitle. 130 Cong Rec S8887, S8888 (June
17 29, 1984)." In re Public Serv Co, 108 BR at 865. See App Leg
18 History (Doc #73) at LH 001, 017, 041.

19 As discussed at length in In re Public Serv Co, 108 BR at
20 863-866, however, the most relevant change to the bankruptcy code
21 for present purposes did not occur in 1984, with the addition of
22 the "notwithstanding" phrase, but in 1978 with the adoption of the
23 Bankruptcy Reform Act of 1978. Before that act, public utilities
24 were required to obtain the approval of the utilities' governing
25 commission before plans of reorganization could be approved. The
26 1978 Reform Act deleted this statutory requirement. A little
27 history is helpful to understand the import of this.

28 Before 1934, corporate reorganization was primarily

1 accomplished through equity receiverships in the federal courts.
2 See 6 Collier on Bankruptcy, 14th Ed, ¶ 0.04 (1978). In 1933 and
3 1934, § 77, governing interstate railroad corporations, and § 77B,
4 governing ordinary corporate debtors, were added by amendments to
5 the Bankruptcy Act of 1898. See id. Section 77B(e)(2) addressed
6 debtor utilities:

7 In case the debtor is a utility subject to the
8 jurisdiction of a regulatory commission or commissions or
9 other regulatory authority or authorities, created by the
10 laws of the State or States in which the properties of
11 the debtor are operated, a plan of reorganization shall
12 not be confirmed until (a) it shall be submitted to each
13 such commission or authority having regulatory
14 jurisdiction over the debtor, (b) an opportunity shall be
15 afforded each such commission or authority to suggest
16 amendments or objections to the plan, and (c) the judge
17 shall consider such amendments or objections at a hearing
18 at which each such commission or authority may be heard.
19 In case the debtor is a public utility corporation wholly
20 interstate in character no court shall approve any plan
21 or reorganization if the regulatory commission of such
22 State having jurisdiction over such public utility
23 certifies that the public interest is affected by said
24 plan, unless said regulatory commission shall first
25 approve of said plan as to the public interest therein
26 and the fairness thereof. If said regulatory commission
27 shall not within thirty days or such additional period as
28 the court may prescribe after the submission of a plan to
it file said certificate it shall be deemed that the
public interest is not affected by said plan.

Reprinted in 6 Collier on Bankruptcy, 14th Ed, ¶ 0.06 (1978).

Section 77B(f) further provided for state approvals
before plan confirmation. The requirement of state approval for
public utility plans of reorganization survived the extensive
amendments to the Bankruptcy Act by the Chandler Act of 1938.
Section 177, in chapter X of the amended act, provided, for
example:

In case a debtor is a public-utility corporation, subject
to the jurisdiction of a commission having regulatory
jurisdiction over the debtor, a plan shall not be
approved * * * until--

- 1 (1) it shall have been submitted to each such commission;
- 2 (2) an opportunity shall have been afforded each such
- 3 commission to suggest amendments or offer objections to
- 4 the plan; and
- 5 (3) the judge shall have considered such amendments or
- 6 objections at a hearing at which such commission may be
- 7 heard.

8 Reprinted in Collier on Bankruptcy, 15th Ed, App Pt 3(a), (2002).
 9 See also § 178 (requiring certification of approval of utility plan
 10 by state commission); § 224 (requiring, "in the case of a public-
 11 utility commission, the procuring of authorization, approval, or
 12 consent of each commission having regulatory jurisdiction over the
 13 debtor" for the taking of "all action necessary to carry out the
 14 plan.").

15 In other words, the bankruptcy code at one time
 16 explicitly provided precisely what the CPUC urges is presently
 17 required to effect PG&E's plan of reorganization. But the
 18 provisions requiring approval by public utility commissions for the
 19 transactions necessary to carry out a utility's reorganization plan
 20 were not made part of the 1978 Reform Act, which, considering the
 21 inclusion of such provisions in the bankruptcy code from its
 22 origin, is a omission that can be inferred to have some
 23 consequence. As the In re Public Serv Co court noted: "After 44
 24 years of requiring state approval for public utility
 25 reorganizations, the statutory law substantially changed with the
 26 adoption of the 1978 Code * * *. There is only one reference in
 27 chapter 11 of the Bankruptcy Code to any utility regulatory agency
 28 approvals and that is for rates." 108 BR at 864, citing §
 1129(a)(6)(discussed below). Moreover, as PG&E points out, the
 1978 Reform Act largely carried forward the regulatory approval
 requirements for railroads. See §§ 1166 and 1172(b)("If * * *
 transfer of, or operation of or over, any of the debtor's rail
 lines by an entity other than the debtor or a successor to the

debtor under the plan would require approval by the Commission under a law of the United States, then a plan may not propose such a transfer or such operation unless the proponent of the plan initiates an appropriate application for such a transfer or such operation with the Commission and * * * the Commission * * * approves such application * * *").

The reason for the removal of state regulatory approval for utility reorganization in the bankruptcy code does not appear to have been discussed in the legislative history accompanying the 1978 Reform Act. It is worth noting, however, that Congress established FERC as an independent agency within the Department of Energy in 1977, see 42 USC § 7171, shortly before enactment of the 1978 Reform Act, and granted that agency an expanded role in the dual sphere of regulation over the provision of energy, codified in the Federal Power Act, 16 USC §§ 824-824m. That the withdrawal of the ability of state regulators to veto reorganization of public utilities in federal bankruptcy proceedings followed closely behind an expanded federal role in the regulation of energy is likely not coincidence.

Nevertheless, notwithstanding a lack of legislative history explicitly discussing Congress' reasoning, the removal of the requirement of approval by state commissions is quite significant. See Muscogee Nation v Hodel, 851 F2d 1439, 1444 (DC Cir 1988) ("where the words of a later statute differ from those of the previous one on the same or related subject, the Congress must have intended them to have a different meaning.").

Only one paragraph of the committee reports accompanying the 1978 Code is devoted to § 1123(a)(5), appearing in both the

House and Senate reports, which reads:

Paragraph 4 [which later became paragraph (5)] of subsection (a) is derived from section 216 of chapter X with some modifications. It requires the plan to provide adequate means for the plans execution. These means may include retention by the debtor of all or any part of the property of the estate, transfer of all or any part of the property of the estate to one or more entities, whether organized pre- or post-confirmation, merger or consolidation of the debtor with one or more persons, sale and distribution of all or any part of the property of the estate, satisfaction or modification of any lien, cancellation or modification of any indenture or similar instrument, curing or waiving of any default, extension of maturity dates or change in interest rates of securities, amendment of the debtor's charter, and issuance of securities.

HR Rep No 595, 95th Cong, 1st Sess 407, (1977); S Rep No 989, 95th Cong, 2d Sess 119 (1977).

This language, if largely by the absence of any reference to the contingency of the specified possibilities on compliance with nonbankruptcy law or regulatory approval, seems to indicate that such actions may be taken--and not just put in a plan-- notwithstanding any nonbankruptcy law. Significantly, this implication seems to have been made explicit in a statement on the floor of the Senate, by Senator DeConcini, chairman of the Subcommittee on Improvements in Judicial Machinery of the Senate Committee on the Judiciary, "in order to explain the House amendment to the Senate amendment to HR 8200." 124 Cong Rec 33992 (Oct 5, 1978). Section 1123, DeConcini noted, "represents a compromise between similar provisions in the House bill and Senate amendment."

Section 1123(a)(5) of the House amendment is derived from a similar provision in the House bill and Senate amendment but deletes the language pertaining to "fair upset price" as an unnecessary restriction. Section 1123 is also intended to indicate that a plan may provide for any action specified in section 1123 in the case of a corporation without a resolution of the board of

1 directors. If the plan is confirmed, then any action
2 proposed in the plan may be taken notwithstanding
3 any otherwise applicable law in accordance with section
4 1142(a) of title 11.

5 Id at 34005, emphasis added.

6 DeConcini's reference to § 1142(a), which imposes a duty
7 on the debtor to carry out the plan "[n]otwithstanding any
8 otherwise applicable nonbankruptcy law, rule, or regulation
9 relating to financial condition * * *," in a discussion of § 1123,
10 would seem on first glance to make his remarks somewhat ambiguous.
11 Section 1142 provides that a reorganized debtor and any newly
12 created entity are obligated to carry out the plan
13 "[n]otwithstanding any otherwise applicable nonbankruptcy law,
14 rule, or regulation relating to financial condition." Section
15 1123(a)(5) governs the obligation of a plan to provide adequate
16 means for reorganization "[n]otwithstanding any otherwise
17 applicable nonbankruptcy law." Read together, these sections
18 direct that the reorganization transactions themselves may be
19 accomplished without hinderance from nonbankruptcy law, but that
20 going forward from bankruptcy, the reorganized debtor and any new
21 entities must comply with all laws in carrying out the
22 reorganization, except those relating to financial condition.

23 Significantly, the very language used by DeConcini, with
24 the insertion of the word "nonbankruptcy," in explaining the House
25 and Senate compromise embodied in the 1978 Reform Act found its way
26 into the act by the 1984 amendment. This may explain why the
27 addition of the "notwithstanding" phrase was characterized as
28 technical and stylistic; the addition of this phrase merely
clarified and reaffirmed the preemptive scope of § 1123(a),

intended by Congress by the enactment of the 1978 Reform Act.

The legislative history, therefore, supports PG&E's interpretation of § 1123(a)(5). But this attention to legislative history, in turn, merely supports the plain language of this section, to which, with this background, the court will now return.

The term "notwithstanding" is well recognized as a term used to express broad preemptive intent. Indeed, as noted by the Supreme Court, courts have long held that a clearer statement of an intent "to supersede all other laws" is "'difficult to imagine.'" Cisneros v Alpine Ridge Group, 508 US 10, 18 (1993), quoting Liberty Maritime Corp v United States, 928 F2d 413, 416 (DC Cir 1991) and citing, among other authority, In re FCX, 853 F2d at 1154. Moreover, the phrase "notwithstanding any otherwise applicable nonbankruptcy law" clearly expresses an intent affirmatively to authorize actions that are otherwise prohibited by nonbankruptcy law, which accords with PG&E's interpretation of the section. The interpretation of the CPUC and the bankruptcy court, however, would not have § 1123(a) authorize otherwise prohibited actions, but would rather have the "notwithstanding" phrase serve a much more limited role, merely clarifying that § 1123(a) is the section that designates what must go into a reorganization plan.

As PG&E correctly notes, the CPUC and the bankruptcy court have trouble coming up with any otherwise applicable nonbankruptcy laws that this phrase would override. The bankruptcy court "imagined" that the statute could preempt a state law that "would prohibit a party from even submitting a plan to the bankruptcy court without first obtaining approval from a debtor's shareholders." Bankr Dec at 18, citing remarks by DeConcini. But

§ 1123(a) does not concern the procedure for submission of a plan to the bankruptcy court; it concerns what must be provided for in a plan. The same defect is present in the bankruptcy court's example of "labor laws that might obligate a plan proponent to negotiate in good faith before submitting a plan." *Id.* The CPUC's examples are no more apt.

The CPUC mentions state statutes "that provide for a dissolving corporation to file a plan of distribution containing specified mandatory elements" and suggests that § 1123(a) merely provides that those statutes "do not govern, and that section 1123(a) alone says what must be in the plan." CPUC Br (Doc #78) at 35. Two interpretations are possible under this account. Either the CPUC would have Congress mean that any other statute that specifies what must go in a reorganization plan is invalid, or the CPUC would have Congress mean that § 1123(a) is an independent supplement to other laws specifying what must go in a reorganization plan. In neither case would Congress have referred to "otherwise applicable" laws. The reference to "otherwise applicable" laws would appear to reflect Congress' intent temporarily to suspend the operation of laws of general applicability, which is not the meaning of the phrase given by the CPUC's interpretation.

The court also thinks it significant that § 1123(a)(5) requires the provision of "adequate means for the plan's implementation" in the plan. If state regulatory approval were required for all the transactions necessary to effect reorganization, how would the debtor, the court or, in the words of the bankruptcy court, "a hypothetical investor typical of holders

1 of claims or interests of a relevant class," know whether the plan
2 provisions were adequate or otherwise "make an informed judgment"
3 about the plan? Bankr Dec at 22. At best, a utility could guess
4 whether what was provided for in a plan would be adequate for
5 reorganization based on an estimate of the chances of regulatory
6 approval. "[S]ince the language of Section 1123 is obviously
7 intended to provide for plans that could go forward for
8 confirmation subject only to the requirements of section 1129--
9 including the rate approval power of a state regulatory agency--it
10 would be nonsensical to interpret Section 1123 to simply list what
11 a plan may include but with the result that such a plan could not
12 be confirmed." In re Public Serv Co, 108 BR at 884.

13 Moreover, other elements of the bankruptcy code support
14 the conclusion that Congress intended to preempt nonbankruptcy laws
15 otherwise applicable to transactions necessary for reorganization.
16 In particular, § 1129(a), which specifies the conditions precedent
17 for approval of the plan by the bankruptcy court, provides that:

18 (a) The court shall confirm a plan only if all of the
19 following requirements are met:
* * *

20 (6) Any governmental regulatory commission with
21 jurisdiction, after confirmation of the plan, over the
22 rates of the debtor has approved any rate change provided
for in the plan, or such rate change is expressly
conditioned on such approval.

23 Congress, in other words, expressly provided that a plan
24 contemplating a rate change by a utility under the jurisdiction of
25 a regulatory commission cannot be confirmed unless the rate change
26 is approved by the appropriate regulatory commission. "[W]here
27 Congress includes particular language in one section of a statute
28 but omits it in another section of the same Act, it is generally

1 presumed that Congress acts intentionally and purposefully in the
2 disparate inclusion or exclusion." INS v Cardoza-Fonseca, 480 US
3 421, 432 (1987). See also United States v Jones, 567 F2d 965, 967
4 (10th Cir 1977)(noting that "if a statute specifies one exception
5 to the general application, other exceptions are excluded * * *").
6 The clear implication of § 1129(a)(6) is that state regulatory
7 approval is not required for plan provisions unrelated to rate
8 changes.

9 The addition of § 1123(d), added by Congress in 1994,
10 which carves out an express limitation to the preemptive effect of
11 § 1123(a), further supports the interpretation that § 1123(a)
12 preempts laws that may obstruct transactions contemplated by a
13 reorganization plan. See Bankruptcy Reform Act of 1994, Pub L No
14 103-394, § 305(a), 108 Stat 4106, 4134. Section 1123(d) provides:

15 Notwithstanding subsection (a) of this section and
16 sections 506(b), 1129(a)(7), and 1129(b) of this title,
17 if it is proposed in a plan to cure a default the amount
18 necessary to cure the default shall be determined in
accordance with the underlying agreement and applicable
nonbankruptcy law.

19 Although the addition of this section arguably calls the
20 specific holding of Entz-White into question, see Southland Corp v
21 Toronto-Dominion, 160 F3d 1054, 1059 n6 (5th Cir 1998), it would
22 indeed seem to confirm a reading of § 1123(a) as expressly
23 preempting laws otherwise applying to plan provisions. On its
24 face, § 1123(d) appears to carve out an exception from the broad
25 preemptive effect of § 1123(a)(5)(G), which governs the curing or
26 waiving of any default in a debtor's plan, by requiring that the
27 amount necessary to cure a default shall be determined by the
28 underlying agreement and applicable nonbankruptcy law. If §

1 1123(a) did not (otherwise) broadly preempt otherwise applicable
2 laws governing, among other things, the curing of any default, the
3 reference in § 1123(d) to "subsection (a)" would make little sense.
4 PG&E's query aptly exposes the strained interpretation given to §
5 1123(d) by the CPUC: "[W]hy would Congress have bothered to
6 prohibit a proponent from merely proposing that a plan accomplish
7 something that the Code bars a plan from actually accomplishing?"
8 PG&E Supp Br at 3, emphasis in original.

9 Finally, the court notes that PG&E's interpretation
10 comports more closely with the purposes of chapter 11 of the
11 bankruptcy code. "The paramount policy and goal of Chapter 11, to
12 which all other bankruptcy policies are subordinated, is the
13 rehabilitation of the debtor." In re Ionosphere Clubs, Inc, 98 BR
14 174, 176 (Bankr SDNY 1989). "The fundamental purpose of
15 reorganization is to prevent a debtor from going into liquidation,
16 with an attendant loss of jobs and possible misuse of economic
17 resources." NLRB v Bildisco & Bildisco, 465 US 513, 528 (1984),
18 citing HR Rep No 95-595, p 220 (1977). As in In re Public Serv Co,
19 "the issue is a narrower one than may first appear." 108 BR at
20 861. PG&E contends that the bankruptcy code expressly prohibits
21 the exercise of a veto power by state regulators over the
22 transactions necessary to reorganize. PG&E's concern that its
23 contemplated reorganization would be thwarted by state regulators
24 is hardly an idle one; the CPUC's discussion of the inadequacies of
25 federal regulation evince an entrenched resistance to relinquishing
26 regulatory jurisdiction over PG&E's operations. See CPUC Br (Doc
27 #78) at 13. But the ability of debtors to reorganize and thereby
28 avoid liquidation under chapter 11 would be severely compromised if

1 state regulators could thwart otherwise adequate means of
2 reorganization. As the New Hampshire bankruptcy court observed:
3 "Corporate reorganization cannot work without substantial
4 restructuring of the corporate entity that is relatively prompt and
5 free from litigation costs and delays and fragmented proceedings in
6 numerous other forums apart from the reorganization court." 108 BR
7 at 890.

8 The preemption issues raised by reorganization are
9 particularly acute in the case of a public utility in bankruptcy,
10 as perhaps no other debtor is subject to as much state regulation
11 as the public utility. But the removal of the statutory right of
12 approval by state commissions of the restructuring of public
13 utilities by the 1978 Bankruptcy Reform Act is powerful evidence
14 that Congress concluded that public utilities should no longer be
15 subject to the costs, delays and uncertainty accompanying such a
16 requirement. The bankruptcy code at one time permitted state
17 regulatory commissions to wield considerable power over the
18 reorganization of public utilities. But now--with the exception of
19 the right to approve rate changes--it does not. Nonbankruptcy laws
20 otherwise applicable to the "restructuring transactions necessary
21 to an effective and feasible reorganization" are expressly
22 preempted by the bankruptcy code. In re Public Serv Co, 108 BR at
23 891.

24
25 III

26 Accordingly, the bankruptcy court's March 18, 2002, order

27 //

28 //

1 disapproving disclosure statement must be REVERSED and the matter
2 remanded for proceedings consistent with this order.

3
4 IT IS SO ORDERED.
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

United States District Court

For the Northern District of California

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

VAUGHN R WALKER
United States District Judge